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No. 05-409

IN THE

Supreme Court of the United States

CARL KIRCHER, *et al.*,

Petitioners,

v.

PUTNAM FUNDS TRUST, *et al.*,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

BRIEF *AMICI CURIAE* OF THE SECURITIES INDUSTRY ASSOCIATION AND THE BOND MARKET ASSOCIATION IN SUPPORT OF PETITIONER

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QUESTION PRESENTED

Whether the court of appeals properly exercised appellate jurisdiction to review the district court's remand order, when the remand order was the result of a substantive decision rejecting a federal statutory preemption defense to certain securities fraud class actions available under the Securities Litigation Uniform Standards Act of 1998.

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INTEREST OF THE *AMICI CURIAE*[1]

The Securities Industry Association ("SIA") brings together the shared interests of approximately 600 securities firms to accomplish common goals. SIA's primary mission is to build and maintain public trust and confidence in the securities markets. SIA members (including investment banks, broker-dealers, and mutual fund companies) are active in all U.S. and foreign markets and in all phases of corporate and public finance. According to the Bureau of Labor Statistics, the U.S. securities industry employs nearly 800,000 individuals, and its personnel manage the accounts of nearly 93 million investors directly and indirectly through corporate, thrift, and pension plans. In 2004, the industry generated $236.7 billion in domestic revenue and an estimated $340 billion in global revenues. (More information about SIA is available at www.sia.com.)

The Bond Market Association ("TBMA") represents approximately 200 securities firms, banks, and asset managers that underwrite, sell, trade, and invest in debt securities and other credit products in the United States and in international markets. Its members include securities dealers and brokers that are large multi-product firms and those with special market niches, as well as asset management firms with over $9 trillion under management. From its inception in 1976, TBMA has worked with its member firms, Congress, the Securities Exchange Commission, the Federal Reserve Board, the Federal Reserve Bank of New York, state regulators, and self-regulatory organizations to foster effective, efficient regulation; to enhance the liquidity and

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[1] Pursuant to this Court's Rule 37.6, *amici* SIA and TBMA state that no counsel for any party authored this brief in whole or in part, and no person or entity other than *amici* and their members made a monetary contribution to the preparation or submission of the brief. Counsel of record for both parties have consented to the filing of this brief, and the letters of consent have been filed with the Clerk.

efficiency of the markets for debt and credit products; to encourage sound credit and business practices for participants in such markets; and to promote the highest levels of professional standards and conduct in such markets. (More information about TBMA is available at www.bondmarkets.com.)

The SIA and/or TBMA have previously filed *amici* briefs with the Court in cases affecting civil liability and the federal securities laws. See, *e.g.*, *Merrill Lynch, Pierce, Fenner & Smith, Inc.* v. *Dabit*, No. 04-1371, 2006 WL 694137 (U.S. Mar. 21, 2006); *Dura Pharms., Inc.* v. *Broudo*, 125 S. Ct. 1627 (2005); *Howsam* v. *Dean Witter Reynolds, Inc.*, 537 U.S. 79 (2002); *Lampf, Pleva, Lipkind, Prupis & Petigrow* v. *Gilbertson*, 501 U.S. 350 (1991); *Rodriguez De Quijas* v. *Shearson/Amer. Express, Inc.*, 490 U.S. 477 (1989); *Shearson/Amer. Express, Inc.* v. *McMahon*, 482 U.S. 220 (1987).

The issue raised by this case is whether the courts of appeals have the authority to review district courts' interpretations of the various questions of federal law that arise in determining whether the preemption defense of the Securities Litigation Uniform Standards Act of 1998, Pub. L. No. 105-353, sec. 101, § 16, 112 Stat. 3227, 3227-33, ("SLUSA" or "Uniform Act") is applicable. This issue is one of great import to the securities industry and investors in this era of proliferating securities litigation. It is critically important to the SIA and TBMA that the effort of Congress to curb vexatious securities litigation by enacting the uniform national requirements of SLUSA not fall prey to plaintiffs who attempt creatively to avoid SLUSA preemption. Uniform standards are critical to the use of U.S. securities markets by both domestic and foreign issuers. Such national uniformity requires that the substantive issues of federal law that arise in determining whether the elements of the SLUSA preemption defense are satisfied be subject to appellate review. *Amici* therefore have a vital interest in the issue

presented in this case, and their views and experience can assist the Court in resolving that issue.

STATUTORY PROVISIONS INVOLVED

Securities Litigation Uniform Standards Act:

> No covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party alleging – (A) a misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security; or (B) that the defendant used or employed any manipulative or deceptive device or contrivance in connection with the purchase or sale of a covered security.

15 U.S.C. § 78bb(f)(1); *accord id.* § 77p(b).

> Any covered class action brought in any State court involving a covered security, as set forth in paragraph (1) of this section, shall be removable to the Federal district court for the district in which the action is pending, and shall be subject to paragraph (1).

15 U.S.C. § 78bb(f)(2); *accord id.* § 77p(c).

General Federal Remand Statute:

> A motion to remand the case on the basis of any defect other than lack of subject matter jurisdiction must be made within 30 days after the filing of the notice of removal . . . . If at any time before final judgment it appears that the district court lacks subject matter jurisdiction, the case shall be remanded.

28 U.S.C. §1447(c).

> An order remanding a case to the State court from which it was removed is not reviewable on appeal or otherwise, except that an order remanding a case to the State court

> from which it was removed pursuant to section 1443 of this title shall be reviewable by appeal or otherwise.

28 U.S.C. § 1447(d).

INTRODUCTION AND SUMMARY OF ARGUMENT

This case presents the question whether the courts of appeals may review a district court's adjudication of a substantive question of federal law – whether the federal defense of SLUSA preemption applies – when the result of that adjudication is to remand a removed securities law class action to State court.

At issue is whether a substantive ruling deciding the merits of a federal defense by a district court, indisputably vested with subject matter jurisdiction by Congress to decide exactly that issue, should receive federal appellate review in consonance with SLUSA's purpose of guaranteeing uniform national standards. As set forth below, a ruling on the merits of the SLUSA preemption defense is not a determination of the district court's subject matter jurisdiction reached before and divorced from the substantive merits. Rather, a determination by a district court that the federal defense of SLUSA preemption is not applicable is a substantive adjudication by that court of the elements of a federal substantive defense. Thus, remand determinations based on such substantive rulings are premised on neither jurisdictional nor procedural grounds, and therefore are not barred from appellate review under the general remand statute, 28 U.S.C. § 1447(d). See, *e.g.*, *Thermtron Prods., Inc.* v. *Hermansdorfer*, 423 U.S. 336, 345 (1976).

Moreover, the Seventh Circuit correctly noted that if remands of SLUSA claims are deemed non-appealable, "major substantive issue[s] . . . will escape review." *Kircher* v. *Putnam Funds Trust*, 373 F.3d 847, 850 (7th Cir. 2004). For example, if the Seventh Circuit had declined to exercise appellate review over a SLUSA-based remand in *Kircher*, it is

unlikely that the vital *Dabit* issue – whether SLUSA preempts holder class actions – would have been decided by this Court because there would have been no conflict in the circuits. *Merrill Lynch, Pierce, Fenner & Smith, Inc.* v. *Dabit*, No. 04-1371, 2006 WL 694137 (U.S. Mar. 21, 2006). Failure to provide federal appellate review to SLUSA remands based on rejection of the preemption defense will result in the balkanization of federal law governing the scope and meaning of the preemption defense to securities actions provided by SLUSA. This would badly undermine the statute's promise of providing "uniform standards" to govern national securities fraud class actions.

ARGUMENT

I. A LOWER COURT'S REJECTION OF SLUSA'S PREEMPTION DEFENSE IS A REVIEWABLE MERITS RULING.

The propriety of appellate review follows from three basic points. *First*, the text of the Uniform Act demonstrates that SLUSA provides a substantive federal defense to covered class actions. A determination that the SLUSA preemption defense applies is therefore a substantive adjudication of the merits that fully disposes of the covered state law class claims. *Second*, such final merits determinations are subject to appellate review. Section 1447(d), read *in pāri materia* with section 1447(c), poses no bar to appellate review of adjudications of a substantive federal defense. *Third*, this Court's recent decision in *Arbaugh* v. *Y & H Corp.*, 126 S. Ct. 1235 (2006), confirms that a ruling is not properly classified as jurisdictional merely because it addresses a threshold, potentially dispositive issue.

A. The Language Of The Uniform Act Demonstrates That SLUSA Provides A Substantive Defense.

The language of the statute makes clear that SLUSA preemption is a federal defense to securities fraud class actions – not a jurisdictional provision. As the Seventh Circuit observed in the decision below, "a federal judge is not only authorized but also required to decide whether *any* court may entertain the litigation" when a SLUSA defense is presented. *Kircher*, 373 F.3d at 849 (emphasis added). The language of the statute is clear that this preemption defense is applicable in *both* federal and state court: "No covered class action . . . may be maintained in any *State or Federal* court." 15 U.S.C. § 78bb(f)(1) (emphasis added); *accord id.* § 77p(b).

Petitioners themselves effectively acknowledge that SLUSA preemption is a merits issue, going to the elements of a substantive defense, and not a jurisdictional issue as to which forum should hear the issue. They do so by conceding that, absent removal, the exact same preemption defense still applies in state court. See Pet. Br. at 47. Indeed, state courts must adjudicate the merits of the SLUSA preemption defense in instances when the removal provision is not invoked. See, *e.g.*, *Shackelford* v. *Ohio Nat'l Life. Ins. Co.*, No. D043503, 2004 WL 2074411 (Cal. Ct. App. Sept. 16, 2004); *Howard Gunty Profit Sharing Plan* v. *Greenwood*, No. B144043, 2001 WL 1190761 (Cal. Ct. App. Oct. 5, 2001); *Breakaway Solutions, Inc.* v. *Morgan Stanley & Co.*, No. Civ. A. 19522, 2004 WL 1949300 (Del. Ch. Aug. 27, 2004), *amended on other grounds*, 2005 WL 3488497 (Del. Ch. Dec. 8, 2005).

If an adjudication of the SLUSA preemption defense were purely a matter of federal subject matter jurisdiction, SLUSA preemption would not be a substantive defense presentable in state court. State courts generally do not adjudicate questions that are properly characterized as issues of strictly federal subject matter jurisdiction. For example, if there is diversity between a plaintiff and a defendant, but the defendant does

not remove, the state court will not address that issue. In contrast, state courts must address SLUSA preemption when a defendant does not remove because it is a substantive defense. Accordingly a federal district court decision that a class action is not preempted by SLUSA is also a substantive adjudication of the federal preemption defense.

This is also basic common sense. In a typical federal case, a ruling that a federal court has subject matter jurisdiction does not dispose of, indeed has no effect on, the substantive claims. For example, a ruling that a court has diversity jurisdiction does nothing to address, much less dispose of, the underlying state law claims. In contrast, a ruling that SLUSA preemption applies requires final dismissal of the state law class action claims and those claims cannot be reasserted as part of a "covered class action" in any federal or state court. That is a quintessential decision on the merits. Final decisions on the merits are classically reviewable on appeal. See 28 U.S.C. § 1291.

B. Adjudications Of Substantive Defenses Are Not Subject To § 1447(d)'s Bar Of Appellate Review.

28 U.S.C. § 1447(d) states: "[a]n order remanding a case to the State court from which it was removed is not reviewable on appeal or otherwise." 28 U.S.C. § 1447(d). Because § 1447(d) must be read in conjunction with § 1447(c), appellate review of remand orders is prohibited only where the district court remands because it lacks subject matter jurisdiction at the time of removal, or due to a procedural defect in the removal process itself. *Thermtron Prods.*, 423 U.S. at 345.[2] Here, the district court did not lack subject

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[2] The essence of the argument made by *Amici Curiae* in Support of Petitioners, Law Professors Arthur R. Miller et al., is that the Court should effectively overrule *Thermtron*. This argument is made notwithstanding this Court's application of the *Thermtron* exception in later cases, including its endorsement and application by a unanimous Court in *Quackenbush* v. *Allstate Insurance Co.*, 517 U.S. 706 (1996).

matter jurisdiction at the time of removal. To the contrary, SLUSA's removal provision explicitly vests the federal courts with the authority to determine the substantive merits of the Uniform Act's federal preemption defense. 15 U.S.C. § 78bb(f)(2); *accord id.* § 77p(c). *Supra*, at 14-17.

The Seventh Circuit correctly characterized SLUSA remands based on the rejection of the preemption defense to be the result of substantive determinations by the district court that "come[] at the end rather than the outset of federal adjudication." *Kircher*, 373 F.3d at 848. Accordingly, the appeals court properly held that § 1447(d), read *in pari materia* with § 1447(c), posed no bar to appellate review of SLUSA remand decisions based on rejection of the preemption defense, because such remands do not result from a lack of subject matter jurisdiction, or a defect in the removal

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The Court has not granted certiorari on this issue, nor has briefing been requested. Moreover, Congress, when enacting SLUSA, was entitled to rely on the teachings of *Thermtron*, *Quackenbush*, and *Carnegie-Mellon University* v. *Cohill*, 484 U.S. 343 (1988), that remand determinations based on non-jurisdictional grounds were reviewable on appeal. *See Cannon* v. *University of Chi.*, 441 U.S. 677, 696-98 (1979) (applying implied right of action standard in place when the statute was enacted). Indeed, assuming for the sake of argument, that this Court were nonetheless to choose to limit *Thermtron* to its facts, and rule that remand determinations based on *substantive* grounds beyond the specific jurisdictional and procedural grounds set forth in 1447(c) could not be appealed, such a ruling should apply only prospectively to actions under new statutes, and not serve as a bar to appellate review of remands based on rejection of SLUSA preemption.

We also note that in addition to the description of Professor Miller's academic interests and treatise cited in his *amici* brief, Professor Miller also frequently serves as co-counsel to some of the nation's largest plaintiffs' class action firms in securities litigation. *See, e.g., Makor Issues & Rights, Ltd.* v. *Tellabs, Inc.*, 437 F.3d 588 (7th Cir. 2006); *In re Cendant Corp. Litig.*, 264 F.3d 201 (3rd Cir. 2001); *In re BankAmerica Corp. Sec. Litig.*, 263 F.3d 795 (8th Cir. 2001); *Helwig* v. *Vencor, Inc.*, 251 F.3d 540 (6th Cir. 2001) (en banc); *Robbins* v. *Koger Props., Inc.*, 116 F.3d 1441 (11th Cir. 1997).

process, but rather from a substantive rejection of the federal defense. *Id.* at 848-49.[3]

The decision of the Seventh Circuit was consistent with this Court's precedent holding that appellate review of remand orders is barred only for those grounds specified in § 1447(c). See, *e.g.*, *Quackenbush* v. *Allstate Ins. Co.*, 517 U.S. 706, 711-12 (1996) (§ 1447(d) did not bar review of remand based on *Burfurd* abstention); *Carnegie-Mellon Univ.* v. *Cohill*, 484 U.S. 343, 347-48 (1988) (discretionary remand of remaining pendent state law claim after federal claim dismissed is reviewable on appeal); *Thermtron Prods.*, 423 U.S. at 351 (remand order based on district court's congested docket reviewable on appeal because it was not a ground for remand specified in § 1447(c)). "*[O]nly* remands based on grounds specified in § 1447(c) are immune from review under § 1447(d)." *Things Remembered, Inc.* v. *Petrarca*, 516 U.S. 124, 127 (1995) (emphasis added). Section 1447(c) does not specify that district courts must remand actions upon the rejection of a federal preemption defense. Accordingly, § 1447(d) poses no bar to appellate review of SLUSA-based remand determinations made on that basis.[4]

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[3] This does not mean that remands in SLUSA cases would necessarily be appealable when the basis for remand was something other than rejection of the SLUSA preemption defense. For example, the remand of a SLUSA-removed case because of the defect that removal was untimely under the 30-day rule would be unreviewable under § 1447(d).

[4] Petitioners argue that the provision of the Class Action Fairness Act ("CAFA"), which specifically authorizes "an appeal from an order of a district court granting or denying a motion to remand a class action to the State court." Pub. L. No. 109-2, § 5(a), 119 Stat. 4, 12 (2005) (to be codified at 28 U.S.C. § 1453(c)(1)), demonstrates that appellate review of SLUSA-based remands is prohibited because SLUSA does not have such a provision. To the contrary, SLUSA does not contain a specific provision authorizing appellate review of SLUSA-based remands because none is required. Remand determinations under SLUSA such as this case are based on substantive adjudications of the merits of the federal defense and were thus appealable under *Thermtron's* controlling, and twice reaffirmed,

C. *Arbaugh* v. *Y & H Corp.* Confirms That A Ruling Is Not Jurisdictional Simply Because It Addresses A Threshold, Potentially Dispositive Issue.

This Court's recent decision in *Arbaugh* v. *Y & H Corp.*, 126 S. Ct. 1235 (2006), confirms that it is error to classify a merits ruling as jurisdictional simply because it addresses a threshold issue that could dispose of the case. *Arbaugh* involved "the distinction between two sometimes confused or conflated concepts: federal-court 'subject-matter' jurisdiction over a controversy; and the essential ingredients of a federal claim for relief."[5] *Id.* at 1238. There the context was whether, following a jury verdict, a Title VII claim was properly dismissed for a newly-raised issue of lack of subject matter jurisdiction. The Court held that the employee-numerosity requirement of Title VII, although a threshold and potentially dispositive issue, related to the "substantive adequacy of Arbaugh's Title VII claim," and as such did "not circumscribe federal-court subject-matter jurisdiction." *Id.*

Arbaugh teaches that the term jurisdiction is not properly invoked to describe all threshold, potentially dispositive rulings. It correctly rejects the category of "drive-by

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interpretation of § 1447(d) when SLUSA was enacted in 1998. In contrast, CAFA requires an express provision to overcome § 1447(d)'s bar of appellate review because remands under CAFA are made on the basis of purely procedural and jurisdictional grounds, which fall within the ambit of § 1447(c), and thus would not be appealable under *Thermtron*.

[5] That the substantive elements at issue here are pertinent to a defense does not negate the fact that the district court, in determining the applicability of SLUSA, adjudicates the substantive merits of a claim for relief. *See Tennessee* v. *Davis*, 100 U.S. 257, 264 (1879) ("A case consists of the right of one party as well as the other, and may truly be said to arise under the Constitution or a law or a treaty of the United States whenever its correct decision depends upon the construction of either. Cases arising under the laws of the United States are such as grow out of the legislation of Congress, whether they constitute the right or privilege, or claim of protection, *or defence of the party*, in whole or in part, by whom they are asserted.") (emphasis added).

jurisdictional rulings" in which courts label threshold merits dismissals as based on "lack of jurisdiction." *Id.* at 1242.

Indeed, if the SLUSA preemption determination by the district court were ruled to be a matter of jurisdiction, it is foreseeable that a situation analogous to that presented in *Arbaugh* would arise. Imagine that a securities fraud class action comprising a mix of claims from the Securities Act of 1933 and state law claims was removed from state court to federal court under SLUSA.[6] Thereafter, the plaintiffs do not challenge removal or preemption, litigate their federal claims, and lose. If a successful SLUSA preemption defense is jurisdictional, plaintiffs could, at that late stage in the litigation, assert that the state claims were improperly preempted and that the entire case should accordingly be remanded to state court for lack of jurisdiction. Indeed, under Petitioners' interpretation of 28 U.S.C. § 1447(d), that end-of-the-case remand would not be appealable. Interpreting SLUSA preemption to be jurisdictional would thus enable class action plaintiffs to game the system, and would result in "unfairness and waste of judicial resources," *id.* at 1245, exactly what *Arbaugh* holds is improper.

II. INTERPRETATION OF REMOVAL AND APPEAL PROVISIONS SHOULD SERVE THE PURPOSE OF THE SPECIFIC SUBSTANTIVE STATUTE AT ISSUE.

Statutory provisions relating to removal should be construed to serve the purposes of the underlying statute, here

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[6] Absent SLUSA, 1933 Act claims are not removable. Securities Act of 1933, ch. 38, § 22, 48 Stat. 74, 86-87 (codified as amended at 15 U.S.C. § 77v); *see also* Jordan A. Costa, *Removal of Securities Act of 1933 Claims After SLUSA: What Congress Changed, and What It Left Alone*, 78 St. John's L. Rev. 1193 (2004). Federal courts have exclusive jurisdiction over civil suits arising under the Securities Exchange Act of 1934, ch. 404, § 27, 48 Stat. 881, 902-03 (codified as amended at 15 U.S.C. § 78aa). Accordingly, when securities plaintiffs sue in state court, they often combine 1933 Act and state law claims.

SLUSA. The interpretation afforded by this Court to the federal officer removal statute, 28 U.S.C. § 1442, is illustrative. Under that statute, suits against federal officers may be removed if a "colorable federal defense" is raised, and like the provision allowing for removal under SLUSA, "despite the nonfederal cast of the complaint; the federal-question is met if the defense depends on federal law." *Jefferson County, Ala.* v. *Acker*, 527 U.S. 423, 431 (1999). In construing the colorable federal defense requirement, this Court has "rejected a 'narrow, grudging interpretation' of the statute, recognizing that 'one of the most important reasons for removal is to have the validity of the defense of official immunity tried in a federal court.'" *Id.* at 431 (quoting *Willingham* v. *Morgan*, 395 U.S. 402, 407 (1969)). Cf. *California Pub. Employees' Retirement Sys.* v. *WorldCom, Inc.* 368 F.3d 86, 103-04 (2nd Cir. 2004) ("[I]n its every detail, Section 1452(a) [the bankruptcy removal statute] is designed to further Congress's purpose of centralizing bankruptcy litigation in a federal forum."), *cert. denied*, 534 U.S. 1080 (2005).

Similarly, the SLUSA removal provision reflects Congress's intent that the merits of the federal preemption defense available under SLUSA be evaluated by the federal courts. SLUSA's purpose of promoting uniformity of national standards to govern securities fraud litigation is furthered by providing federal appellate review to all district court adjudications of SLUSA preemption, and not only to pro-preemption rulings that result in dismissal of the claim.

A. SLUSA Aims To Ensure That Uniform National Standards Govern Securities Fraud Litigation.

"The magnitude of the federal interest in protecting the integrity and efficient operation of the market for nationally traded securities cannot be overstated." *Merrill Lynch*, No. 04-1371, 2006 WL 694137, at *4. As apparent from its very title, the purpose of SLUSA is to achieve national "uniform standards" for "securities litigation." SLUSA makes the

federal antifraud provisions for securities litigation, which are governed by the Private Securities Litigation Reform Act of 1995 (Reform Act or PSLRA),[7] the exclusive national standard for most securities fraud class actions.

In passing the Uniform Act, Congress paid heed to testimony that "[n]ational [securities] markets should . . . be governed by national standards." *Oversight Hearing on Securities Litigation Abuses Concerning S. 1260, The Securities Litigation Uniform Standards Act of 1997, Before the Subcomm. on Sec. of the S. Comm. on Banking, Hous., and Urban Affairs*, 105th Cong. 67 (1997). "If individual States are permitted to assert individual jurisdiction over transactions in national markets, the predictable result is chaos and mayhem." *Id.* at 79. SLUSA sought to protect businesses from exposure to litigation in each of the fifty states under fifty different procedural and substantive standards when such litigation could arise in the event of a single allegation of fraud in connection with the purchase or sale of a nationally traded security.

In particular, SLUSA's legislative history indicates that as foreign securities markets grow, this makes it increasingly important to ensure uniformity and certainty in the U.S. securities markets. 143 Cong. Rec. S10475, S10477 (daily ed. Oct. 7, 1997), *available at* 1997 WL 614735 ("[I]f our markets are to remain ahead of those in London, Frankfurt, Tokyo or Hong Kong, we must create uniformity and certainty."). See also *id.* ("How can we expect to get foreign companies to list on our exchanges if we have to explain that they will face not only our very tough Federal standards on securities fraud, but also the possibility of 50 constantly changing State standards").

Congress explained the reasons behind the enactment of SLUSA in § 2 of the statute. Pub. L. No. 105-353, § 2, 112

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[7] Pub. L. No. 104-67, 109 Stat. 737 (1995) (codified as amended in scattered sections of 15 U.S.C.)

Stat. at 3227. Specifically, Congress found, *inter alia*, that "since enactment of [PSLRA], considerable evidence has been presented to Congress that a number of securities class action lawsuits have shifted from Federal to State Courts," *id.* § 2(2), 112 Stat. at 3227; "this shift has prevented [PSLRA] from fully achieving its objectives," *id.* § 2(3), 112 Stat. at 3227; and that

> in order to prevent certain State private securities class action lawsuits alleging fraud from being used to frustrate the objectives of [PSLRA], it is appropriate to enact *national* standards for securities class action lawsuits involving nationally traded securities, while preserving the appropriate enforcement powers of State securities regulators and not changing the current treatment of individual lawsuits.

Id. § 2(5), 112 Stat. at 3227 (emphasis added).

The Uniform Act aimed to "prevent plaintiffs from seeking to evade the protections that Federal law provides against abusive litigation by filing suit in the State court, rather than Federal, court." H.R. Rep. No. 105-803, at 13 (1998) (Conf. Rep.) The legislation was

> designed to protect the interests of shareholders and employees of public companies that are the target of meritless "strike" suits [the purpose of which] is to extract a sizeable settlement from companies that are forced to settle, regardless of the lack of merits of the suit, simply to avoid the potentially bankrupting expense of litigating.

Id.

B. SLUSA's Purpose Is Undermined By Allowing Preemption Decisions That Result In Remand To Evade Appellate Review.

SLUSA guarantees that uniform national standards govern national securities litigation by making federal courts,

applying federal law, the exclusive venue for certain securities class actions. 15 U.S.C. § 78bb(f)(1); *accord id.* § 77p(b). Thus, for "covered class actions"[8] that fall within the scope of SLUSA's preemption provision, the sole remedy available for investors is a federal securities fraud action, where plaintiffs must comply with the heightened pleading standards and other procedural safeguards provided by PSLRA.[9]

Congress reinforced SLUSA's guarantee of uniformity for securities litigation by including a statute-specific removal provision that vests federal courts with the authority to make the substantive determinations required to establish SLUSA's preemption defense. 15 U.S.C. § 78bb(f)(2); *accord id.* § 77p(c). SLUSA's removal provision effectively serves as a statutory exception to the well-pleaded complaint rule, which would otherwise preclude removal to federal court of a state law claim when the only basis for removal was assertion of a federal defense. See *Caterpillar* v. *Williams*, 482 U.S. 386, 392 (1987). By providing for removal of securities class actions, Congress plainly sought to ensure that *federal* courts

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[8] A "covered class action" is defined as a lawsuit "in which . . . damages are sought on behalf of more than 50 persons or prospective class members," 15 U.S.C. § 77p(f)(2)(A)(i)(I); or where "one or more named parties seek to recover damages on a representative basis on behalf of themselves and other unnamed parties similarly situated," *id.* § 77p(f)(2)(A)(i)(II); or "any group of lawsuits filed or pending in the same court and involving common questions of law or fact in which (I) damages are sought on behalf of more than 50 persons; and (II) the lawsuits are joined, consolidated, or otherwise proceed as a single action for any purpose, *id.* § 77p(f)(2)(A)(ii).

[9] For example, under the Reform Act's heightened pleading standards, plaintiffs are required to "state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind." 15 U.S.C. § 78u-4(b)(2). PSLRA also provides for an automatic stay of discovery upon the filing of a motion to dismiss. *Id.* § 78u-4(a)(3); *accord id.* § 77z-1(a)(3).

would develop the precedent on the scope of SLUSA's preemption defense.

It would be contrary to Congress's plan to bar appellate review of district court preemption determinations under SLUSA only where the district court *rejects* preemption and permits state law claims to go forward. To disallow appellate review only for district court decisions that permit state law claims increases the likelihood of the very balkanization of securities law standards that SLUSA is designed to prevent.

It further disserves the substantive uniformity that SLUSA promotes to have a lopsided system where: (a) decisions favoring preemption are immediately reviewed by a federal court of appeals, but (b) decisions rejecting preemption will usually never be subject to appellate review because the vast majority of remanded cases will settle in the state trial courts regardless of their legal merits.[10] Such a lopsided system

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[10] This Court has repeatedly noted its concern of the effect on securities markets of settlements that are disproportionate to the legal merits of the claim. *See, e.g., Merrill Lynch*, No. 04-1371, 2006 WL 694137, at *5; *Dura Pharms.* v. *Broudo*, 125 S.Ct. 1627, 1634 (2005); *Central Bank of Denver, N.A.* v. *First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 189 (1994). As Congress recognized when designing the PSLRA: "If a defendant cannot win an early dismissal of the case, the economics of litigation may dictate a settlement even if the defendant is relatively confident that it would prevail at trial." S. Rep. No. 104-98, at 7 (1995) (internal quotation marks omitted); *see also* J. Alexander, *Do the Merits Matter? A Study of Settlements in Securities Class Actions*, 43 Stan. L. Rev. 497, 578 (1991) ("virtually all cases are settled"). Senator Phil Gramm described the situation prior to the passage of SLUSA:

> [W]e were able to pass a piece of legislation [PSLRA] aimed at doing something about this problem. We have had many companies, especially new growth companies, plagued with abusive lawsuits, often being forced to settle out of court because of the high costs of proving innocence. We had a system of parasites who were literally bleeding the life blood out of growth companies in America . . . .
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> . . . .

would thwart SLUSA's central purpose by "evad[ing] the protections that Federal law provides against abusive litigation by filing suit in the State court, rather than Federal court." H.R. Rep. No. 105-803, at 13.

C. The Lack Of Appellate Review Of Decisions Rejecting SLUSA Preemption Would Eviscerate SLUSA's Goal Of National Uniformity.

Failure to exercise appellate review over SLUSA-based remand determinations has already resulted in a proliferation of unreviewed, and often conflicting, district court decisions. This fragmentation of the case law and the absence of any controlling precedent eviscerates the "uniform" federal defense to securities fraud class actions that is promised by SLUSA.

Except for the Seventh Circuit's decision to exercise appellate review over a SLUSA-based remand in *Kircher*, and the resulting creation of a conflict between the Second and Seventh Circuits, it is unlikely that the important *Dabit* issue – whether SLUSA preempts holder class actions – would ever have come to the Court's attention. *Merrill Lynch*, No. 04-1371, 2006 WL 694137, at *2. The *Dabit* issue is but one of many substantive questions of federal law that are being adjudicated across the country as district courts

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> . . . We discovered . . . that a new loophole was being exploited, that what was occurring is that there has been a shift of these lawsuits into State courts.

Oversight Hearing on Securities Litigation Abuses Concerning S. 1260, The Securities Litigation Uniform Standards Act of 1997, Before the Subcomm. on Sec. of the S. Comm. on Banking, Hous., and Urban Affairs, 105th Cong. 1-2 (1997) (statement of Senator Phil Gramm). In short, SLUSA was

> designed to protect the interests of shareholders and employees of public companies that are the target of meritless "strike" suits [the purpose of which] is to extract a sizeable settlement from companies that are forced to settle, regardless of the lack of merits of the suit, simply to avoid the potentially bankrupting expense of litigating.

H.R. Rep. No. 105-803, at 13.

exercise their jurisdiction in determining whether the elements of the federal defense provided by SLUSA are satisfied. If the courts of appeals could not review district court rejections of SLUSA's preemption defense, the statute's goals of uniformity and consistency in the application of federal securities law would never be realized.

As one district court judge has lamented, "the district court cases appear to be all over the map on the issue of what state law claims are preempted by SLUSA." *Magyery* v. *Transamerica Fin. Advisors, Inc.*, 315 F. Supp. 2d 954, 959 (N.D. Ind. 2004). At issue in *Magyery* was whether SLUSA-preemption requires a state law complaint to allege that the defendants made a misrepresentation or omission of material fact with scienter. The court chronicled the "clear split among the courts on the issue of whether the . . . claims must allege 'scienter' for SLUSA preemption to apply." *Id.* at 959-60 (comparing *Burns* v. *Prudential Secs., Inc.*, 116 F. Supp. 2d 917 (N.D. Ohio 2000) (requiring scienter), and *Green* v. *Ameritrade, Inc.*, 120 F. Supp. 2d 795, 798 (D. Neb. 2000) (same), *aff'd on other grounds*, 279 F.3d 590 (8th Cir. 2002), and *Shaw* v. *Charles Schwab & Co.*, 128 F. Supp. 2d 1270, 1272-73 (C.D. Cal. 2001) (same), with *Winne* v. *Equitable Life Assur. Soc'y of the United States*, 315 F. Supp. 2d 404, 413-15 (S.D.N.Y. 2003) (SLUSA preemption does not require scienter)).

The district courts are similarly struggling with other substantive issues that arise in defining the "national standards for securities class action lawsuits involving nationally traded securities" promised by SLUSA. H.R. Rep. No. 105-803, at 2. Such issues include, *inter alia*:

1) How to arrive at the "50 persons" total for the purposes of establishing a "covered class action" under 15 U.S.C. § 77p(f)(2)(A)(ii). Compare *In re WorldCom, Inc. Securities Litigation*, 308 F. Supp. 2d 236, 246 (S.D.N.Y. 2004) (holding ten individual actions collectively brought on behalf of more than 50 persons that were subsequently consolidated

in federal court, and containing the same claims constituted a "group of lawsuits" and was therefore a "covered class action" and noting that the absence of any indication in SLUSA that the joined actions be pending in the same *state* court), with *In re Enron Corp. Sec., Derivative & "ERISA" Litig.*, No. MDL-1446, 2002 WL 32107216, at *5 (S.D. Tex. Aug. 12, 2002) (holding that conditions for SLUSA preemption, including consolidation of actions, must exist at time of removal from state court);

2) Whether SLUSA's definition of a "covered class action" encompasses state law actions seeking equitable relief, rather than traditional damages. See, *e.g.*, *Feitelberg* v. *Merrill Lynch & Co.*, 234 F. Supp. 2d 1043 (N.D. Cal. 2002) (holding that restitution and disgorgement damages sought under state law qualify as monetary damages for purposes of SLUSA removal), *aff'd*, 353 F.3d 765 (9th Cir. 2003) (per curiam); *Gibson* v. *PS Group Holdings, Inc.*, No. 00-CV-0372, 2000 WL 777818 (S.D. Cal. June 14, 2000) (holding that class action plaintiff may not defeat removal by omitting a prayer for damages);

3) How the Uniform Act's preemption defense should apply to complaints that include a mixture of preempted and non-preempted claims. Compare *Greaves* v. *McAuley*, 264 F. Supp. 2d 1078 (N.D. Ga. 2003) (holding that because certain claims were excepted from SLUSA preemption under the "Delaware carve-out," 15 U.S.C. § 77p(d)(4), entire action should be remanded), with *Gray* v. *Seaboard Secs., Inc.*, 241 F. Supp. 2d 213, 219-20 (N.D.N.Y. 2003) (determining SLUSA preemption as to each separate claim), *rev'd in part on other grounds*, 126 F. App'x 14 (2nd Cir. 2005); and

4) How strictly to read complaints in determining whether the elements of the SLUSA preemption defense are satisfied – in particular, whether or not district courts should limit themselves to assessing allegations made on the face of the complaint and, relatedly, the extent to which plaintiffs should be allowed to plead around the elements of the SLUSA

preemption defense. See generally Jennifer O'Hare, *Preemption Under the Securities Litigation Uniform Standards Act: If It Looks Like a Securities Fraud Claim and Acts Like a Securities Fraud Claim, Is It a Securities Fraud Claim?*, 56 Ala. L. Rev. 325, 348-68 (2004) (surveying conflicting case law).

This list is only illustrative of the myriad questions of federal law, beyond the *Dabit* issue, that arise in district courts as they contend with the merits and scope of SLUSA's federal preemption defense. Indeed, Petitioners themselves devote several pages of their brief to chronicling various substantive issues regarding SLUSA preemption, beyond the issue this Court has now addressed in *Merrill Lynch, Pierce, Fenner & Smith, Inc.* v. *Dabit*, No. 04-1371, 2006 WL 694137 (U.S. Mar. 21, 1006). See Pet. Br. at 42-45.

It is therefore clear that absent appellate review of district court rejections of SLUSA preemption, SLUSA's promise of uniformity will prove to be merely illusory. In promulgating the Uniform Act, Congress surely did not intend to allow erroneous district court interpretations of the reach of purportedly uniform national standards to remain uncorrected. Nor did Congress intend for federal appellate courts to be hamstrung in their role of resolving conflicts between differing district court interpretations of the scope of the SLUSA preemption defense. But these will be exactly the outcomes of a failure to allow appellate review of SLUSA-based remands. If rejections of SLUSA preemption are deemed non-appealable, then "major substantive issue[s] . . . will escape review." *Kircher*, 373 F.3d at 850. SLUSA's purpose of encouraging capital formation in U.S. markets by mandating uniform federal standards for securities class actions can be achieved only if *all* district court rulings on the merits of the federal defense provided by SLUSA, including those that result in remands to state court, are subject to federal appellate review.

CONCLUSION

For the foregoing reasons, the judgment of the Seventh Court of Appeals should be affirmed.

Respectfully submitted,

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